

STAFF PAPER

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Accounting Standards Advisory Forum

Project	Leases		
Paper topic	Project Update		
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33. Sitzung IFRS-FA am 02.12.14
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Introduction and objective of the meeting

1. The objective of this paper is to provide the Accounting Standards Advisory Forum (ASAF) members with an update on the status of the Leases project, including a summary of the previous ASAF discussions on leases since September 2013.

Project Update

2. Since the September 2014 ASAF meeting, the IASB and the FASB (the boards) have continued to redeliberate the proposals in the 2013 *Leases* ED. In October 2014, the boards discussed the definition of a lease and confirmed the principle in the 2013 ED, ie a lease exists when the customer controls the use of an identified asset for a period of time. The boards agreed to clarify that the definition of a lease generally requires a customer to have (a) the right to direct how and for what purpose the leased asset is used throughout the period of use, and (b) the right to substantially all of the economic benefits from directing the use of the leased asset. In essence, a lease exists when the customer has exclusive use of an identified asset for a period of time and can decide how to use it.
3. In addition, the boards discussed whether the definition of a lease should also require a customer to have the ability to derive the benefits from directing the use of an identified asset on its own or together with other readily available resources. The boards' discussion indicated that adding such a requirement would be

expected to result in little difference in the scope of the new *Leases* standard.

Some board members also raised concerns about unintended consequences. The boards instructed the staff to consider feedback from members of both boards and to bring the issue back to a future joint board meeting.

4. The main topics remaining to be discussed are lessee disclosures and transition requirements.
5. In Appendix A of this paper, we include a summary of the discussions on leases held at ASAF meetings in September 2013, December 2013, March 2014 and September 2014, and the related tentative decisions reached by the IASB since March 2014.

ASAF discussion topic	Summary of the ASAF discussions	Related IASB tentative decisions
September 2013		
<p>Discussion of major topics within the 2013 ED</p> <ul style="list-style-type: none"> • Lessee accounting model • Lessor accounting model • Measurement of lease assets and liabilities (including the determination of the lease term) • Definition of a lease • Disclosure and transition 	<p>Lessee accounting model</p> <p>ASAF members broadly supported the proposal that lessees should recognise assets and liabilities arising from leases on the balance sheet. ASAF members had mixed views about the proposed dual approach to recognising lease expenses. Some members were concerned about the complexity that results from having a dual approach. Some members noted that, although they have conceptual concerns about the proposed dual approach, they understand the IASB’s and FASB’s reasoning for developing it and, accordingly, could accept it in order to achieve the recognition of assets and liabilities arising from leases on a lessee’s balance sheet. Some members encouraged the boards to develop a single lessee accounting model, with amortisation and interest recognised separately for all leases. They thought there could be more support for such a model if the boards narrowed the scope, such as by broadening the application of the proposed short-term lease exemption. One member, however, cautioned the boards about any such broadening of the short-term lease exemption. Many ASAF members recommended the IASB to reduce complexity and cost further to ensure a much better cost/benefit trade-off.</p>	<p>Lessee accounting model</p> <p>The boards have tentatively decided that a lessee would recognise assets and liabilities arising from all leases, with some exemptions (ie short term leases and small asset leases).</p> <p>The IASB has tentatively decided to adopt a single lessee model that would require the recognition of interest and amortisation for all leases recognised on a lessee’s balance sheet.</p> <p>In response to concerns about cost and complexity, the boards have simplified the measurement of lease assets and liabilities. Consequently, variable payments and most optional payments would be excluded from that measurement.</p> <p>The boards have also simplified the reassessment requirements compared to those proposed in the 2013 ED (detailed later), thereby reducing the cost and complexity of application.</p> <p>In addition, the boards have clarified that a lessee can apply the requirements to a portfolio of similar leases, rather than to each individual lease.</p>

ASAF discussion topic	Summary of the ASAF discussions	Related IASB tentative decisions
	<p>Lessor accounting model</p> <p>ASAF members had mixed views. Some members suggested not changing the existing lessor model, some supported a single model and others thought the extent of the risks associated with the residual should be considered in determining the appropriate lessor model.</p>	<p>Lessor accounting model</p> <p>The boards have tentatively decided, in essence, to leave lessor accounting unchanged, and to enhance disclosure about a lessor’s exposure on asset risk.</p>
	<p>Other topics</p> <p>ASAF members also raised specific points for the boards’ consideration about measurement of lease assets and liabilities, the definition of a lease, disclosure and transition. In particular, suggestions were made about clarifying and simplifying the determination of the lease term.</p>	<p>Lease term</p> <p>To reduce costs of implementation of the new standard, the boards tentatively decided to:</p> <ul style="list-style-type: none"> • retain the terminology in existing leases guidance (ie ‘reasonably certain’ in IAS 17 <i>Leases</i>) in assessing whether to include optional periods in the lease term; and • require a lessee to reassess the lease term only upon the occurrence of a significant event or a significant change in circumstances that is within the control of the lessee.

ASAF discussion topic	Summary of the ASAF discussions	Related IASB tentative decisions
December 2013		
Discussion about the feedback received on the 2013 ED and next steps on the project.	ASAF members asked how they could help with the next steps on the project. The IASB indicated that they would hope to obtain ASAF members' views on the costs and benefits of the various possible paths forward at the next ASAF meeting and, in the meantime, would be available for individual meetings with ASAF members by video.	---
March 2014		
Discussion of ways forward for lessee and lessor accounting and the possible simplifications to the 2013 ED for the following topics: <ul style="list-style-type: none"> • Lessee accounting model • Small-ticket leases • Lessor accounting model • Measurement • Separation between lease and non-lease components. 	<p>Convergence</p> <p>As a general comment, one ASAF member commented that the convergence of accounting standards on leases between IASB and FASB is critically important, and suggested that both boards should not abandon this important objective, having regard to the significant amount of efforts over the past years.</p>	<p>Convergence</p> <p>The boards are continuing to discuss the project jointly, with the aim of minimising any differences between IFRS and US GAAP. The boards have reached different tentative decisions on the lessee model and a few other topics.</p>
	<p>Lessee accounting model</p> <p>Most ASAF members indicated their preference for a single model that would require a lessee to recognise and present amortisation and interest separately for all leases. These members thought that such a model would avoid complexity and result in more relevant information for investors and analysts.</p>	<p>Lessee accounting model</p> <p>The IASB has tentatively decided to adopt a single lessee model that would require the recognition of interest and amortisation for all leases recognised on a lessee's balance sheet.</p>

ASAF discussion topic	Summary of the ASAF discussions	Related IASB tentative decisions
	<p>Definition of a lease</p> <p>Some ASAF members said that the most important topic to be addressed during further redeliberations was the scope of the new Standard, including the definition of a lease. They noted in particular that consideration should be given to excluding contracts that in substance are for the provision of services.</p>	<p>Definition of a lease</p> <p>The boards have tentatively decided to retain the principle in the 2013 ED, ie a lease exists when the customer controls the use of an identified asset for a period of time. The boards have clarified various aspects of the lease definition guidance that would help entities to identify a lease and ensure that a lease is recognised only when the lessee controls the right to use an asset.</p>
	<p>Small-ticket leases</p> <p>Some ASAF members strongly encouraged the IASB to try to identify a measure which would strike the right balance between the incremental costs and benefits. Other ASAF members stated that any simplifications should not inadvertently actually cause complexity, and some suggested that they may not be needed at all, because of the existing materiality guidance in IFRS.</p>	<p>Small-ticket leases</p> <p>To address concerns about the costs to apply the proposals to large volumes of small items, the boards have (a) changed the definition of a short-term lease to be consistent with the determination of the lease term and (b) clarified that a lessee can apply the requirements to a portfolio of similar leases, rather than to each individual lease. The IASB is also considering an exemption for leases of small assets (such as laptops and office furniture).</p>

ASAF discussion topic	Summary of the ASAF discussions	Related IASB tentative decisions
	<p>Lessor accounting model</p> <p>Most ASAF members supported retaining guidance similar to that in existing IFRS, which would require Type A accounting for leases for which the residual value is insignificant. Some ASAF members viewed an approach based on the lessor’s business model as attractive but did not advocate such an approach at this time. An ASAF member suggested a lessor ROU model that is consistent with the lessee ROU model but that would allow the lessor to measure the residual asset at fair value, similarly to investment properties.</p>	<p>Lessor accounting model</p> <p>The boards have tentatively decided, in essence, to leave lessor accounting unchanged, and to enhance disclosure about a lessor’s exposure on asset risk.</p>
	<p>Measurement</p> <p>ASAF members had mixed views but generally supported simplifying the reassessment requirements in the 2013 ED.</p>	<p>Measurement</p> <p>The boards have simplified the reassessment requirements compared to those proposed in the 2013 ED as follows:</p> <ul style="list-style-type: none"> (a) a lessee would reassess the lease term only upon the occurrence of a significant event or a significant change in circumstances that is within the control of the lessee; and (b) a lessee would reassess inflation-linked variable lease payments only when the contractual cash payments change (not at each reporting date)

ASAF discussion topic	Summary of the ASAF discussions	Related IASB tentative decisions
	<p>Separation of lease and non-lease components</p> <p>ASAF members expressed support for simplifications, but some had concerns about separating lease and non-lease components. It was noted that this could be a less important issue if service contracts were excluded from the scope. There was agreement that the observable stand-alone price threshold in the 2013 ED should be reconsidered.</p>	<p>Separation of lease and non-lease components</p> <p>The boards tentatively decided to allow a lessee to use estimates (in the absence of, or in addition to, observable information) when separating payments between lease and service components in a contract.</p>
September 2014		
<p>Discussion of the status of the project and a paper prepared by EFRAG staff on the definition of a lease.</p>	<p>Definition of a lease</p> <p>The EFRAG staff paper suggested changes to the proposed guidance on the definition of a lease as follows:</p> <p>(a) define a lease as a financing arrangement for the right-of-use asset for a period of time; and</p> <p>(b) to align the guidance on unbundling lease and service components with the guidance on unbundling in the Revenue Recognition Standard.</p> <p>ASAF members had mixed views on the suggestions included in the EFRAG staff paper.</p> <p>Regarding defining a lease as a financing arrangement, the following views were expressed</p> <p>(a) One member fully supported the IASB retaining its</p>	<p>Definition of a lease</p> <p>The boards considered the suggestions made in the EFRAG staff paper at the October 2014 joint board meeting (refer to “financing component approach” and “IFRS 15/Topic 606 approach” sections of agenda paper 3A of the October 2014 joint board meeting).</p> <p>The boards agreed not to modify the definition of a lease by requiring that a lease is a financing arrangement for the right to use an asset.</p> <p>The boards discussed whether the definition of a lease should also require a customer to have the ability to derive the benefits from directing the use of an identified asset on its own or together with other readily available resources. The boards instructed the staff to consider feedback from members of both boards and to</p>

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	<p>definition and did not support basing the definition on financing.</p> <p>(b) One member supported the general aim of the financing suggestion, noting that mentioning financing would be helpful in distinguishing leases from services that require the use of assets.</p> <p>(c) Although agreeing that leases are often a form of financing, some members expressed the view that it is more appropriate to define a lease by focusing on obtaining a right of use. One member noted that, in a fully prepaid lease, there is no financing element. Nonetheless, assuming that a lessee obtains a right to use an asset, the transaction should be accounted for as a lease.</p> <p>(d) IASB members expressed concern about focusing on the form of the contract rather than on the substance. This could lead to many existing leases, including finance leases, no longer being considered to be leases. One member also expressed concern about the consequences for lessors.</p> <p>(e) Some members expressed concern about the suggestion to analyse the supplier business model as an indicator of the provision of financing. In their view, the business model of the lessor should not be of critical importance in assessing whether the transaction provides financing for a lessee, particularly for real</p>	<p>bring the issue back to a future joint board meeting.</p>

ASAF discussion topic	Summary of the ASAF discussions	Related IASB tentative decisions
	<p>estate leases.</p> <p>Regarding unbundling different components of a contract, ASAF members generally supported consistency in outcomes between the Leases Standard and the Revenue Recognition Standard.</p>	
	<p>Separation of lease and non-lease components</p> <p>A view was expressed that it might be appropriate to account for an entire contract as a service (ie not to unbundle) when the service component of a contract is substantially larger than the lease component.</p>	<p>Separation of lease and non-lease components</p> <p>The boards considered this suggestion at the October 2014 joint board meeting (refer to “substantial services approach” section of agenda paper 3A of the October 2014 joint board meeting).</p>
	<p>Convergence</p> <p>Finally, some ASAF members noted the importance of convergence between the IASB and FASB on leases.</p>	<p>Convergence</p> <p>The boards are continuing to discuss the project jointly, with the aim of minimising any differences between IFRS and US GAAP. The boards have reached different tentative decisions on the lessee model and a few other topics.</p>